CORPORATE STRATEGY AND PARENTING ADVANTAGE

How parent companies can create – or destroy – value in their constituent businesses

Michael Goold, Andrew Campbell, and Marcus Alexander are directors of the Ashridge Strategic Management Centre in London. Over the last ten years they have placed a considerable research focus on "multibusiness" companies in North America, Europe and Japan. Among the 15 primary companies with whom they undertook joint research are ABB, Banc One, Canon, General Electric, Hanson, 3M, Shell and Unilever. In their 1994 book *Corporate-Level Strategy: Creating Value in the Multibusiness Company,* they brought together the results of that research, and outlined a new approach to the management of multibusiness companies, based on the goal of "parenting advantage": "being the best parent for each of the businesses in the corporate portfolio". More recently, and based on continuing research, they have reiterated the importance of the underlying concepts they proposed.

Fundamentally, the authors suggest that the key question for multibusiness companies – companies whose constituent businesses are diverse in nature and operate in several different marketplaces – is not which businesses to be in, nor how to structure them, nor what size they should be; but rather how the parent can create a strategy which will add value to the constituent businesses.

Corporate Strategy

"Increasing enthusiasm for diversification and multibusiness companies during the 1960s and 1970s, built on concepts of decentralisation, general management skills, synergy and portfolio balance, has been replaced in the 1980s and early 1990s with scepticism about the results achieved by diversified companies, a return to core businesses, and a renewed search for the key to corporate strategy." As the management bandwagons roll by, what distinguishes the successful multibusiness companies from the value-destroyers is their ability to focus clearly on the concept of parenting advantage.

Goold and his fellow authors believe that corporate strategy revolves around two key questions: where should a company invest its resources (portfolio issues of diversification, acquisitions, disposals), and how should the company relate to the businesses it controls (issues of outsourcing, decentralising, restructuring and so on)? Few companies can articulate what their corporate strategies are, except as an aggregation of their constituent businesses' strategies, least of all most multibusiness companies, with their record of destroying shareholder value and of stifling enterprise. Demergers, takeovers and buy outs tend to prove emphatically how much better businesses can do when released from the dead hand of corporate headquarters. But it does not have to be that way, and corporate strategies which add value can be created. Finding a useful role for the parent, or as the authors put it, "the quest for parenting advantage", is key to ensuring that businesses not only perform better in aggregate than they would individually, and that the parent generates sufficient extra value to pay its way, but also that the parent becomes an active source of corporate competitive advantage.

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Parenting Styles

During their research the authors have found that companies can be categorised according to the degree of influence they exercise on planning and control. Those companies that focus on short-term financial targets ("tight financial control") can be contrasted with those that emphasise strategic goals and competitive position, and who are less concerned about financial measures ("flexible control"); and in turn with those that control tightly but try to strike a balance between financial and strategic targets ("tight strategic control"). By looking at the control influence and the degree to which parents become involved in planning and decision-making, three clear parenting styles emerge (see Figure 1).

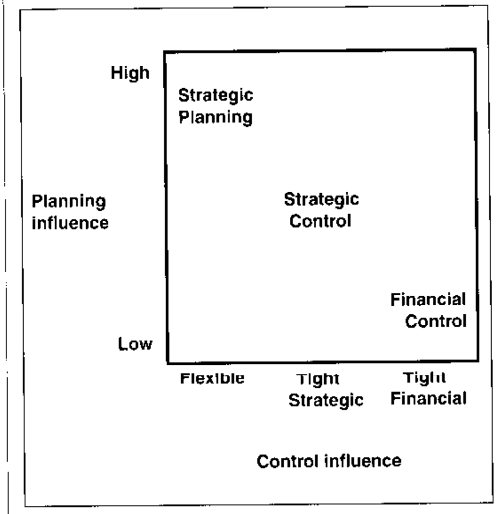

Figure 1: Parenting styles

	Nature of Decisions	Nature of Portfolio Linkages	Nature of Competitive Environment	Nature of Strategy
Strategic Planning	Big, risky, long term	Many/complex	Open or fierce	"Build"
Strategic Control	←	"Middle Ground"		→
Financial Control	Small, incremental, short term	Few/simple	Stable	"Harvest" or turnaround

Figure 2: Businesses that fit best with different styles

The differing styles place differing demands on operating businesses and corporate parents alike. One style may be more or less appropriate according to whether the constituent businesses are in a stable or fluid competitive market; whether there is much interaction between the businesses; whether the businesses are mature or embryonic; whether decisions tend to be fast, frequent and minor or long-term, major and occasional (see Figure 2).

Thus the demerger of ICI, for example, enables the two constituents, ICI and Zeneca, to adopt styles that are appropriate to the differing issues they face in pharmaceuticals and agrochemicals versus those they face in general chemicals.

Generally companies have the option either of changing their parenting style or, more realistically, of focusing their company away from businesses where their current style would be inappropriate and give rise to undue tensions.

The Parenting Advantage Framework

Parenting advantage is "the ability to create more value than rival parents", say the authors. This can be achieved in two ways: either by "seeing more or better opportunities for performance enhancement, or from being better qualified to realise these opportunities". The characteristics of the parent and its businesses must fit well together if value is to be generated. On the one hand are the parent's mental maps (the commonly held views, thought processes, and attitudes of its key staff), the systems and processes, structures and functions, people and resources; whilst on the other hand, the businesses are clearly defined, provide particular opportunities for improvement, and possess critical success factors. But, as the authors point out, it is not enough to have a degree of fit or to avoid significant misfits. The fit must be better than rival parents. It must also take account of future fit – something that requires an appreciation of future trends and alternative scenarios. This all leads to decisions about the portfolio – acquisitions, divestments, alliances – and about the structuring of the parent itself – management levels, processes and systems (see Figure 3).

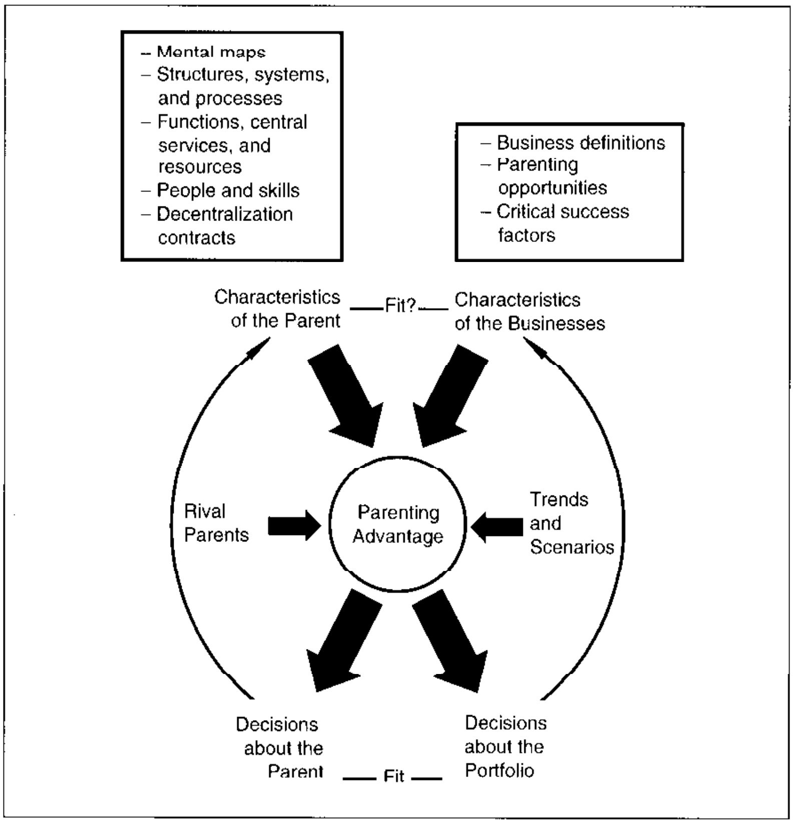

Figure 3: Corporate strategy framework

This framework enables the authors to create what they call a parenting advantage statement for any given company. They refer to the ability of a parent to unlock value by concentrating on particularly important opportunities as "value creation insights". Such an insight might, for example, be the knowledge that in mature manufacturing businesses cost recovery is crucial, because typically managers are reluctant to raise prices. They refer to a consistently supportive and powerful parenting approach as "distinctive parenting characteristics". These might include the ability to assimilate small decentralised businesses into a global network, for instance. And finally, they define business areas to focus on as "heartland businesses", where their parenting skills can generally be expected to bring some benefit.

The authors extend this analysis to enable decisions to be made about the businesses which comprise the portfolio. Companies may decide to keep some businesses that fall outside the heartland in their portfolios. These may be "ballast" businesses that

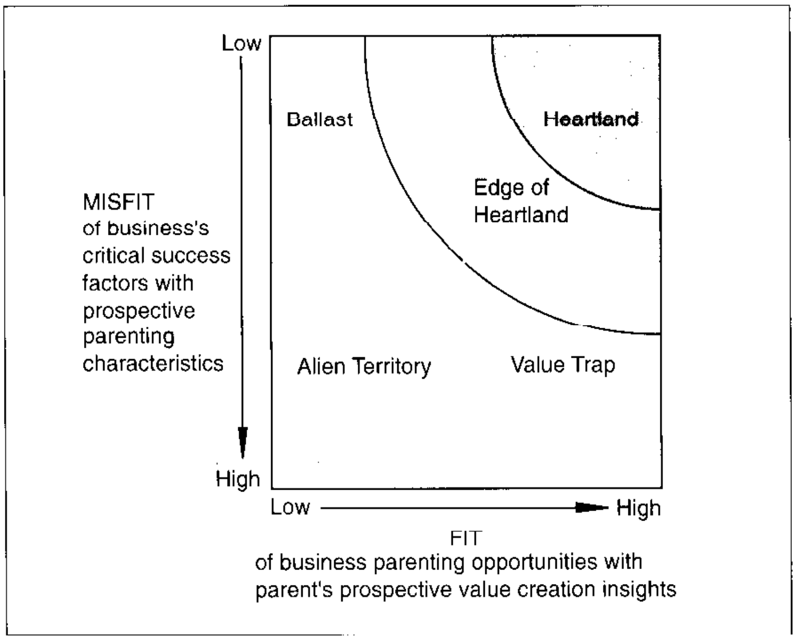

Figure 4: Parenting Fit Matrix

continue to be worth more to the company than to other rivals, or they may be "platform" businesses that are retained to provide a future stepping stone for a changed corporate strategy. However, in the authors' view, "companies with large and growing heartlands should concentrate their efforts on the heartland businesses, where their chances of creating value are likely to be the best." (See Figure 4).

How Parents Create Value

The writers identify four main approaches to value creation, each of which carries with it real risks of destroying value but also the potential for a sound corporate strategy (see Figure 5). They are:

- Stand-alone influence, with the parent improving the individual performance of the businesses
- Linkage influence, whereby the parent improves the links between businesses
- Functional and services influence, which occurs when the parent provides cost effective central services and functional management
- Corporate development activities, with the parent improving the organisation by changing the constitution of the business portfolio

Stand-alone influence This is exerted by all parents, even if only in the form of setting modest financial controls and targets, together with the appointment of key staff. Greater involvement on the part of the parent can take the form of influencing decisions on product market strategies, pricing decisions and human resource development. Whilst the authors view this influence as vital in most companies, they have found it to be a strangely neglected strategic tool. The influence can also be easily abused, by setting inappropriate targets, by making the wrong appointments, or by denying businesses the necessary funds for investment. Moreover, there exists what the authors refer to as the "10% versus 100% paradox", with the experts in the business units giving 100% of their time to that business, being second guessed or overruled by parents who are only able to devote 10% of their time to that business unit, and who are consequently markedly less well informed.

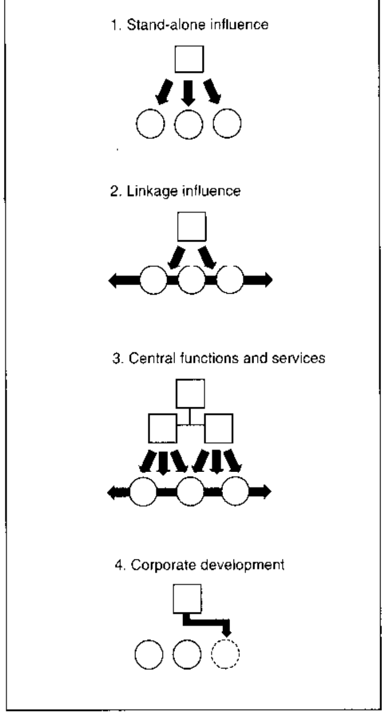

Figure 5: Four types of parental value creation

Linkage influence Parents try to generate extra value by promoting relationships between business units, creating synergy so that the whole company is worth more than the sum of its parts. In this case, the authors have found that the attempts by parents to generate value by encouraging links are generally disappointing, with inappropriate policies and economically unjustifiable initiatives making synergistic benefits elusive. Again they suggest an "enlightened self interest" paradox, pointing out that if capable and motivated business unit managers are unable to see and exploit mutually advantageous linkages between business units, how can parents profess to discern such benefits?

Functional and services influence Many companies believe that centrally resourced corporate functions and services can be made to add value to the whole organisation. In some cases, such functions and staff groups can provide an essential, expert, and cost-effective resource which it would be uneconomic for any one business unit to try to provide for itself. More often than not, though, bureaucracy, cost and irrelevance combine to make such overhead departments deeply unpopular with the business units they profess to serve. The current trend to slim them down and outsource the necessary functions and services is usually justified.

This leads to what the authors call the "beating the specialists" paradox – if a specialist external supplier, which lives or dies by its ability to provide timely cost effective expertise, is available, how can a parent create value by attempting to provide the same service?

Corporate development activities Lastly, the parent can create value by adjusting its portfolio of businesses, through acquisitions and disposals, choosing which businesses to grow organically and which to run down. It can seek out new opportunities, identify businesses for sale that are underpriced, or find ways to make existing businesses more competitive. But the authors have found that in these activities parents are more likely to destroy value than create it, in which case the paradox they face is that they are so unlikely to create value that they shouldn't be allowed to try.

Conditions for Value Creation

The paradoxes outlined above show just how difficult it is for parents to create value through their efforts. Yet some companies manage to overcome the obstacles and come up with strategies that do add value. How? The authors suggest three key factors. First, the constituent businesses must be capable of real performance improvements, and the parent must be able to spot those opportunities and see how it can help deliver them. Secondly, the parent must have particular relevant attributes, such as mental maps, structures, functions or people, that enable it to exploit those opportunities. And lastly, the parent must not be destroying value elsewhere with misguided parenting attempts at a greater rate than it is creating it.

Conditions for Advantage

The last series of conditions that ensure a company can create more value than its rivals are that the parent should possess value creation insights which set it apart; that it should have distinctive parenting characteristics which are more suitable for exploiting opportunities than those of its competitors; and that it should understand more clearly than its rivals how those insights and characteristics can best be applied – in other words, it should know what its heartland businesses are.

Current Thinking

Since the publication of their book in *1994, Goold, Campbell and Alexander* have updated their thinking in an article published in the April 1998 issue of *Long Range Planning*. They believe that the bulk of their research findings still holds true but, if anything, their views on the capacity of the parent to destroy value by interfering appear to have hardened. They point out how business managers filter the information provided to their parents, who thus have even less reliable information on which to base their interventions. They advocate that parents should steer well clear unless they are certain that they can make a positive contribution. The search for synergies, in particular, carries the risk that two capable and focused businesses pursuing separate lives can be reduced to muddle-headed confusion by well-meaning parents encouraging them to search for common ground.

They point out that an assessment of parenting competence is usually of far more use than a voguish analysis of core business competences, and an organisation attempting to follow another management fad and create 'best practice' central services and functions will generally be disappointed with the results. A more idiosyncratic approach will serve a company's unique parenting situation better.

Multibusinesses are, by definition, diverse but the good ones have a notable commonality of parenting needs and opportunities, and focus on the heartland. The ability to stretch parenting skills to meet new opportunities is usually more limited than parents anticipate, and takes longer to achieve.

Lastly, they stress the need to define business unit boundaries and corporate reporting structures clearly and carefully. "Analysis of the advantages of breadth versus focus in business definition and of the impact of different structures on corporate value creation should underpin these organisational choices," not history, ambition or politics ■

REFERENCE: *Michael Goold, Andrew Campbell and Marcus Alexander, "Corporate-Level Strategy: Creating Value in the Multibusiness Company", John Wiley and Sons Inc, 1994, ISBN 0-471-04716-3, £24.95 HB; Michael Goold, Andrew Campbell and Marcus Alexander, "Corporate Strategy and Parenting Theory", Long Range Planning, Vol 31 No 2, 1998.*

COMMENT

Goold, Campbell and Alexander's thinking has been widely seen as an important contribution to the whole subject of corporate strategy in multibusinesses. Based as it is on careful research over a period of years and detailed analysis of the results, it is a heavyweight piece of work and it shows. Anecdotally, people who have worked in the organisations covered in the research provide reassuring comments about the accuracy of the findings, viz: "I have worked for one of the companies to which they refer and their characterisation of its parenting relationship and style is spot on."

Given that the authors' views have been criticised elsewhere for taking too negative a view of parents, and their propensity to destroy rather than create value, it is particularly interesting that nothing has made them change their minds on this issue. Arguably, the title of the book could have been "Minimising Parental Interference" since this is a recurrent element in the authors' search for ways to maximise parenting advantage.

The enjoyable part of the debate that the three Ashridge authors set up is the reversal of the time-honoured question of 'what businesses should we be in?' into an altogether fresher one: 'What type of parent would best suit the business we *are* in?' No doubt it is a good job that there is no such thing as free choice in the matter, otherwise there are plenty of SBUs that would be voting with their feet. Unfortunately, it is for the shareholders to recognise how and where the centre is adding value and, from where they sit, that is difficult to do. Generally, the potential for destroying value is only recognised *after* the event, when it is already too late.

In the longer run, it will be interesting to see how the developing resource-based view of strategy (see pages 6-9) impinges on some of the established conclusions that Goold, Campbell and Alexander have drawn. That new approach to strategy is already touching on the logic behind diversification and the potential for creating strategic assets across and between SBUs – both of direct relevance to parenting issues.